

To summarize: (a) cable prices, properly adjusted to reflect changes in the quantity and quality of programming, are not rising faster than inflation and, (b) programming costs are not primarily responsible for even the nominal increases in cable prices that have taken place since 2002.

III. RETRANSMISSION CONSENT DOES NOT HARM COMPETITION OR CONSUMERS

Professor Rogerson and JCC assert retransmission consent imposes costs on consumers by enhancing the “dominance of the major broadcast networks,”³² who leverage their market power by bundling their “must have” local broadcast channels with MVPD network programming to “force MVPDs to (1) pay higher prices for program networks that they might have purchased in any event and (2) purchase additional program networks that they would not otherwise have purchased.”³³ Moreover, and “most importantly,” according to Rogerson, “this will likely damage competition by either preventing the entry of competitors or at least weakening them,”³⁴ which “may be one of the primary motives for bundling in the first place.”³⁵ Moreover, he argues at length, the Commission has already endorsed this view in its Fox/DirecTV.

As we explain in detail below, each and every aspect of this argument is faulty, either factually, analytically or both. Broadcasters are by no meaningful measure “dominant” in MVPD programming. They do not “force” MVPDs to carry additional networks, but instead offer the alternative of payment for broadcast channels on a stand-alone basis. They do not have “market power” in the sense of being able to force

³² Social Cost at 10.

³³ Social Cost at 50.

³⁴ Social Cost at 51.

anticompetitive or supracompetitive prices or terms on MVPDs; rather, to the extent bundling takes place, it is motivated by efficiency concerns. And, as the Commission has pointed out previously, its findings in Fox/DirectTV unequivocally *do not* support the findings being urged upon it by Professor Rogerson and the JCC.

A. Network Broadcasters Are Not “Dominant” in the Market for MVPD Programming

Professor Rogerson claims that “The four major broadcast networks are now collectively the predominant suppliers of satellite-delivered networks.”³⁶ But in fact, broadcaster MVPD owned-networks are far from dominant in any meaningful sense of the word.

According to the FCC’s most recent report on competition in the MVPD sector, the 89 broadcast-owned cable networks “represent 23 percent of the 388 total networks identified, and 30 percent of the 299 networks that are unaffiliated with a cable operator.”³⁷ Moreover, the Commission found, the number of new networks is growing: “Since our last *Report*, the total number of national networks has increased. In 2004, we identified 388 satellite-delivered national programming networks, an increase of 49 networks over the 2003 total of 339 networks. Of the 388, 89 networks (23 percent) were vertically-integrated with at least one cable operator in 2004. Last year, 110 networks were vertically integrated (33 percent) of the 339 total.”³⁸

³⁵ Social Cost at 51.

³⁶ Social Cost at 17.

³⁷ *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, Eleventh Annual Report* (MB Docket No. 04-227, February 4, 2005), at ¶148. (Hereafter MVPD Report.)

³⁸ MVPD Report at ¶145

As a result, the Commission concluded, “[I]t appears there is diverse ownership of the most popular networks: 10 different entities own all or part of the top 20 programming networks in terms of subscribership.”³⁹

Even the statistics presented by Professor Rogerson do not support his argument. According to his calculations, no entity owns more than 21 percent of MVPD programming networks; the four major broadcast networks taken together own only 56.5 percent;⁴⁰ six cable MSOs own 25.9 percent; and, unaffiliated programmers own 17.6 percent. These figures are far more consistent with the Commission’s findings of diverse and unconcentrated ownership than with Rogerson’s assertion of “dominance.” Indeed, we used Professor Rogerson’s market share statistics for 2004 to calculate a Herfindahl-Hirschman Index (HHI) of 1219,⁴¹ which lies at the bottom end of the “moderately concentrated” range, and is not significantly different from the 1097 HHI figure the FCC estimates for MVPD distributors.⁴² In other words, even using Professor Rogerson’s figures, the MVPD programming industry and the MVPD distribution business are approximately equally “concentrated.”⁴³

³⁹ MVPD Report at ¶150.

⁴⁰ It should be noted that we do not endorse Professor Rogerson’s methodology for calculating market shares. He attributes partial ownership to total market shares – e.g., if a broadcast company owns 10% of a cable network, then 10% of that cable network’s revenues are attributed to the broadcast company (see Social Costs, n.3). There is no reason to believe, however, that a 10% share accords the owner of the network sufficient control (or even influence) to affect strategic behavior. The Commission takes a different approach to calculating shares. See MVPD Report at ¶144, n. 648.

⁴¹ We relied on the figures in Rogerson’s Table 2, p. 8, leaving out the 13 percent total market share attributed to “Others.” Since the individual shares of each of the “others” are small, this omission will have no significant impact on the HHI calculation.

⁴² MVPD Report at ¶144.

⁴³ This is true, of course, only at the national level. At the level of local markets, the distribution business typically is comprised of only three competitors – cable and the two satellite MVPDs – with HHIs in excess of 3000 (i.e., well above the DOJ Guidelines threshold of 1,800 for a “highly concentrated” industry). The FCC classifies only 3.7 percent of downstream MVPD markets as “competitive.” MVPD Report at ¶136.

These structural characteristics of the MVPD marketplace imply that broadcasters should not be able to negotiate higher license fees from MVPD networks than other MVPD programmers. Not surprisingly, this is precisely what the General Accounting Office concluded when it conducted an econometric study of this precise issue in 2003.⁴⁴ That study found that “ownership affiliations – with broadcasters or cable operators – had no influence on cable networks’ license fees.”⁴⁵

B. The Commission’s Fox-DirectTV Analysis Does Not Support Professor Rogerson or the JCC’s Position

Professor Rogerson’s next argument is founded on his insistent misinterpretation of the Commission’s findings in the Fox/DirectTV order. There, Rogerson says, the Commission found that there are not close substitutes for local broadcast content, and that News Corp. therefore had some bargaining power in its negotiations with MSOs.⁴⁶ Professor Rogerson makes much of this finding, which he insists supports his conclusion that broadcasters are able to use retransmission consent to raise prices and/or force un-economic contractual provisions on MSOs.

In fact, the Commission has repeatedly found precisely the opposite to be true. In a passage from the Fox/DirectTV order that appears just a few pages prior to the passages cited by Professor Rogerson, the Commission found that:

⁴⁴ General Accounting Office, *Issues Related to Competition and Subscriber Rates in the Cable Television Industry* (GAO-04-8, October 2003). (Hereafter “GAO 2003.”)

⁴⁵ GAO 2003 at 29. Professor Rogerson attempts to explain away this result in a lengthy footnote, but offers no substantiation for any of his speculative criticisms. Rogerson also points out that the GAO study finds evidence that program networks offered by broadcasters are more likely to be carried by MVPDs than unaffiliated program networks, a fact he says is consistent with his contention that broadcasters use retransmission to get cable operators to carry their networks. Rogerson neglects to mention, however, that the GAO study finds that *programming networks affiliated with cable operators* are also more likely to be carried than unaffiliated networks. This result may be explained as easily by efficiency concerns as by market power – i.e., it may be that both broadcasters and cable operators enjoy economies of scope or other cost advantages that make them more efficient producers and/wholesalers of cable programming.

⁴⁶ Social Cost at 24-27 citing Fox/DirectTV order at ¶¶201, 202, 203.

Both programmer and MVPD benefit when carriage is arranged: the station benefits from carriage because its programming and advertising will likely reach more households when carried by MVPDs than otherwise, and the MVPDs benefit because the station's programming adds to the attraction of the MVPD subscription to consumers. Thus, the ***local television broadcaster and the MVPD negotiate in the context of a roughly even 'balance of terror'*** in which the failure to resolve local broadcast carriage disputes through the retransmission consent process potentially damages each side greatly in their core business endeavor.⁴⁷

As clear as this language would seem to be, it did not prevent commenters in the Commission's recent *a la carte* proceeding from attempting to take out of context some of the same language relied upon by Professor Rogerson. Thus, the Commission took pains in its report to Congress to clarify its finding:

All differentiated products, such as video programming, possess some degree of market power in the sense that there are no perfect substitutes. The critical question in any analysis involving differentiated products is whether the existing degree of market power is sufficient to allow the firm to profitably engage in the hypothesized anticompetitive activity.... ***Thus, nothing in the analysis of the News Corp./DirecTV transaction should be read to suggest that the Commission has concluded that the market power of broadcasters is sufficient to lead to competitive harms in the absence of vertical integration.***⁴⁸

In view of this extremely clear statement, there is simply no justification for Professor Rogerson's insistence that "the Commission's conclusion that broadcasters have market power ... implies that retransmission consent allows broadcasters to

⁴⁷ *In the Matter of General Motors Corporation and Hughes Electronics Corporation, Transferors and The News Corporation Limited, Transferee for Authority to Transfer Control, Memorandum Opinion and Order* (MB Docket No. 03-124, January 14, 2004), at ¶180. (emphasis added). See also ¶75 ("We agree with the Applicants that the instant transaction does not present horizontal concentration issues. The Commission has previously held that broadcast television is not sufficiently substitutable with the services provided by MVPDs to constrain attempted MVPD price increases, and hence, is not in the same relevant product market.") (Hereafter "Fox/DirecTV Order.")

⁴⁸ *Report on the Packaging and Sale of Video Programming Services to the Public* (November 18, 2004), p. 70 (emphasis added). (Hereafter "A La Carte Report.") This language appears in the same paragraph as several sentences cited by Professor Rogerson.

negotiate significant compensation from MVPDs ... [and] means that retransmission consent regulations create a significant social cost.”⁴⁹

Nearly as remarkable as Professor Rogerson’s persistence is the irony inherent in JCC’s attempt to argue that the Fox/DirecTV order has implications for this proceeding, when these same filers (plus Cable One) went out of their way in that proceeding to insist that the issues there were “unique,” “singular” and unrelated to any “rulemaking proceeding.” “The issues raised by the Joint Cable Commenters are transaction specific,” they said.

The fact that [retransmission negotiation] issues may touch upon generic concerns regarding retransmission consent and sports programming costs is of no moment, since ***it is the DirecTV acquisition itself that increases News Corp’s incentive and ability to wield undue pricing power and bargaining leverage*** in connection with its broadcast stations and RSNs....

Moreover, in this instance there [sic] no rulemaking proceeding that addresses the issues raised by the Joint Cable Commenters. Indeed, no other entity has ever owned and operated the unique combination of broadcast network, local stations, cable programming, and multichannel distribution assets involved in this transaction. ***It is the very singularity of the asset combination involved here that triggers the competitive and consumer harms raised by the Joint Cable Commenters*** and others in connection with this transaction.”⁵⁰

In fact, JCC said then, in the absence of the merger, News Corp. would be constrained by uncertainty if it tried to exercise market power in retransmission negotiations:

Prior to acquiring a controlling interest in DirecTV, News Corp. faces some risk and uncertainty [in retransmission consent negotiations]. It does not know whether the loss of subscription and advertising revenue from a service interruption arising from a temporary bargaining impasse with a cable operator over carriage of RSN or FOX programming could be made

⁴⁹ Social Cost at 26.

⁵⁰ Letter from Bruce D. Sokler to Marlene H. Dortch, *Notice of Ex Parte Participation in MB Docket No. 03-124* (August 4, 2003), at 11-12. (The “Joint Cable Commenters” in that proceeding were the same as here, except that Cable One was also among the commenters in the earlier proceeding.)

up via higher carriage fees gained from that distributor (and others in adjacent markets) once the impasse is resolved.⁵¹

In other words, in the absence of vertical integration, broadcasters cannot know whether they have an upper hand in the negotiations or not.

Finally in this context, we note that if their investigation of Fox/DirecTV had caused antitrust authorities to have concerns about joint ownership of broadcast and MVPD programming properties, they had ample opportunity to act on those concerns in the Spring of 2004, when they reviewed the merger of broadcaster GE/NBC with the cable and other entertainment properties of Vivendi's Universal Entertainment Group. But, despite the fact that concerns about the impact of the merger on retransmission negotiations were explicitly raised, the deal cleared antitrust reviews in both the European Union and the United States without any conditions being imposed. Final approval was granted in April 2004, just four months after the FCC's order in Fox/DirecTV.⁵²

C. Anecdotal Evidence that Broadcasters and MVPDs Sometimes Fail to Reach Agreement Does Not Imply Broadcasters Have Market Power

Professor Rogerson seeks to portray the bargaining that goes on between broadcasters and MVPDs as one-sided, citing instances in which negotiations between programmers and broadcasters have led to a temporary impasse, and arguing that

⁵¹ Sokler Letter at 3-4. Professor Rogerson's report in the DirecTV/Fox merger also focused on the increased market power Fox allegedly would enjoy "because the lasting losses to the rival MVPD resulting from the fact that that customers shift to DirecTV will become lasting gains for News Corp., the owner of DirecTV." See William P. Rogerson, *An Economic Analysis of the Competitive Effects of the Takeover of DirecTV by News Corp.*, (June 13, 2003).

⁵² See Jayne O'Donnell, "NBC Vivendi Merger Hits Possible Snag," *USA Today* (December 31, 2003) (available at http://www.usatoday.com/money/media/2003-12-31-merger_x.htm, viewed March 18, 2005); see also Letter from Susan Creighton, Director, Bureau of Competition, to Brackett B. Denniston, General Counsel, General Electric, (April 20, 2004) (available at <http://www.ftc.gov/os/closings/staff/040420ge.pdf>, viewed March 18, 2005).

these anecdotes are evidence that broadcasters have the superior position in the negotiations by virtue of their “must have” programming.⁵³

Negotiations between broadcasters and MVPDs can perhaps accurately be characterized, as the Commission has put it, as a “balance of terror.”⁵⁴ But the notion that cable operators are lacking in bargaining leverage and thus are always forced to capitulate to broadcasters is at variance with the facts.

For example, as this is written, Cox Communications and the Washington Post Company are in an extended dispute with Nextar Broadcasting over carriage of Nextar’s CBS- and NBC-affiliated local broadcast stations in four markets (Abilene, San Angelo, and Texarkana, Texas, and Joplin, Missouri). Nextar pulled its signals off the four cable systems effective January 1, 2005, insisting on some form of financial compensation for carriage of its programming. If Professor Rogerson were right – that broadcasters have substantial market power over MVPDs – we would have expected the cable systems to accede quickly to Nextar’s demands. Instead, after three months, the dispute continues. As the Commission predicted, both sides are suffering from the impasse, but certainly there is no evidence that the cable systems are suffering more. Indeed, according to a report in *Broadcasting & Cable*, the impasse has led to a 40 percent increase in demand for television “rabbit ears” (which have also been offered for free by the cable companies), and forced Nextar to reduce its advertising rates by 30 percent.⁵⁵

⁵³ Social Cost at 20-21.

⁵⁴ News Corp/DIRECTV, at ¶180.

⁵⁵ See John M. Higgins and Bill McConnell, “No Cash, No Carry,” *Broadcasting & Cable* (February 7, 2005) (available at <http://www.broadcastingcable.com/index.asp?layout=articlePrint&articleID=CA501628>, viewed March 21, 2005). It should be noted that at last one of the stations, KRBC Channel 9 in Abilene, is available on the Dish Network – a fact which, according to Professor Rogerson, should further weaken the bargaining

Companies involved in such negotiations may also seek to strengthen their negotiating positions by leveraging the legal/political/regulatory process, as was the case in recent licensing negotiations between Cox and ESPN.⁵⁶ In May 2003, Cox Communications Chairman James Robbins testified before the Senate Commerce Committee in favor of legislation that would force companies like Disney/ESPN to offer their programming *a la carte*. At the time, Cox was nearing the end of its carriage agreement with ESPN, and the *a la carte* proposal was seen as a way for Cox to increase its bargaining leverage vis-à-vis ESPN in the negotiations.

In March 2004, after the negotiations had been successfully completed, Mr. Robbins appeared again before the Committee, but this time testified that *a la carte* was “not in consumers best interests.” Noting this surprising change in position, Chairman McCain queried Mr. Robbins: “When did you find yourself on the road to Damascus?” Chairman McCain asked.

“As soon as [ESPN President] Mr. Bodenheimer got real in his pricing,” Mr. Robbins replied. “My efforts last spring to move ESPN ... to a tier was to get the attention of the Walt Disney Company and bring them to reasonable levels of prices.”⁵⁷

One might draw several conclusions from these episodes, but the most obvious is that both broadcasters and cable companies have multiple weapons in their negotiating arsenals, from giving away free rabbit ears to lobbying Congress (or the

power of the local cable system and lead to a quick capitulation. See www.krbctv.com, viewed March 23, 2005.

⁵⁶ While the Cox-ESPN negotiations did not involve broadcast retransmission consent, the episode nonetheless illustrates clearly how public policy can become a negotiating tool in such situations.

⁵⁷ Hearing Of The Senate Commerce, Science, and Transportation Committee, “Escalating Cable Rates: Causes And Potential Solutions,” *Federal News Service* (March 25, 2004), at 32-33.

FCC) for new regulations. But to argue, as Professor Rogerson does, that one side has disproportionate leverage is simply at variance with the facts.⁵⁸

D. The Offering of a Bundle of Broadcast and MVPD Programming Reflects Economies of Scope and Other Efficiencies, Not Market Power

While Professor Rogerson refers repeatedly to “bundling” and “tie-ins,” at least some broadcasters do not engage at all in tying (i.e., the refusal to sell their broadcast programming unless cable operators also carry their MVPD programming), and engage in only the most innocuous form of bundling (i.e., they offer discounts on sales of multiple products).⁵⁹ Moreover, as Professor Rogerson has argued in other contexts, it is well established in the economics literature that bundling is often economically efficient. Indeed, in his report in the *a la carte* proceeding, Professor Rogerson offers a spirited defense of the practice:

Standard economic theory suggests that some bundling and tiering of programming is likely to be efficient, that the precise form of the efficient tiering scheme is likely to depend in complex ways on market conditions that cable systems will understand better than regulators, and that cable systems will generally have an incentive to choose efficient tiering schemes because cable systems can charge subscribers higher prices by providing them with packages of services they value more highly.⁶⁰

⁵⁸ The notion that broadcasters gain materially from owning MVPD networks is also challenged by Viacom Chairman Sumner Redstone's proposal to break the company into two separate divisions, thereby separating the CBS network and stations from Viacom's MTV Network cable networks. Redstone's rationale is that MTV's affiliation with CBS *lowers* its market capitalization, a conclusion that is explicitly contrary to Professor Rogerson's “leveraging” theory. See John Higgins, “Double Your Pleasure: Viacom Chairman Redstone Explains His Plan to Split Up an Empire,” *Broadcasting & Cable* (March 21, 2005) at 18-19. (“Redstone says that, today, MTV is locked up in a company that trades at around eight times annual cash flow, a relatively low valuation. ‘Separated, I believe, it will have a multiple of 16. That alone is an enormous change.’”)

⁵⁹ On the practices of the broadcasters, see Comments of the Walt Disney Company in this proceeding. This form of bundling is often referred to as “mixed bundling.” See Barry Nalebuff, *Bundling, Tying and Portfolio Effects: Conceptual Issues*, United Kingdom, Department of Trade and Industry (February 2003), at 13-17. (Hereafter “Nalebuff 2003.”)

⁶⁰ William P. Rogerson, “Cable Program Tiering: A Decision Best and Properly Made by Cable System Operators, Not Government Regulators,” (November 10, 2003), at 6. (Hereafter “Tiering.”) Professor Rogerson acknowledges that his view of bundling is different in the two proceedings, and says the difference is due to the fact that “The economic motivations that MVPDs have to bundle programming at the retail level are very different than the economic motivations that explain the type of bundling that

...
[I]t seems likely that profit maximizing firms will generally have an incentive to bundle products efficiently. This is simply because they can charge consumers more money by providing them with packages that better fill their needs.⁶¹

...
[E]ven a firm with market power will generally want to supply its customers with their most preferred mix and packaging of products because it will be able to charge consumers the highest possible price by so doing.⁶²

...
Allowing government to regulate how firms with market power bundle products will only increase the likelihood that the firms do not offer the most efficient bundle of products, but will not prevent them from charging monopoly prices for whatever bundles of products they do sell.⁶³

Needless to say, Professor Rogerson takes a different view of bundling when it is undertaken by broadcasters in their negotiations with cable companies, arguing that the broadcasters are using bundling to “leverage” their market power over one good (broadcast channels) into markets for related goods (cable networks).⁶⁴ Specifically, based on an article by Michael D. Whinston,⁶⁵ he argues that “it seems likely that an additional motivation broadcasters may have to bundle retransmission consent together with other network programs is to capture larger market shares from their potential competitors and thereby either foreclose them from entering entirely or at least weaken them.”⁶⁶

occurs in the case of bundling of retransmission consent together with cable channels at the wholesale level.” (See Tiering at n. 65.) Nowhere, however, does he explain why.

⁶¹ Tiering at 10-11.

⁶² Tiering at 11.

⁶³ Tiering at 12.

⁶⁴ Social Cost at 47. In the preceding section, Professor Rogerson offers a several possible explanations for why both the cable operators and the broadcasters may have preferred “in kind” compensation to cash compensation for retransmission. While some of these explanations may well be valid, they have little or nothing to do with whether the practice enhances or detracts from consumer welfare.

⁶⁵ Michael D. Whinston, “Tying, Foreclosure, and Exclusion,” *American Economic Review* 80:4 (September 1990), 837-859.

⁶⁶ Social Cost at 48.

But neither the Whinston article nor the broader literature on bundling suggests that the conditions in the MVPD programming market are conducive to anticompetitive bundling. Whinston's result, for example, is described by Professor Rogerson as showing that bundling can be effective as a means of leveraging market power when at least one of the bundled products is characterized by increasing returns to scale. Since television production is indeed characterized by increasing returns, he concludes that is what must be happening here.

But Whinston's result applies only in a very narrow set of circumstances which do not appear to apply to this market;⁶⁷ and, in general, the circumstances in which bundling may be used to achieve anticompetitive ends are extremely limited, especially, as here, when at least one of the markets involved is fully competitive.⁶⁸ Certainly, Professor Rogerson does not demonstrate that the conditions for anticompetitive bundling are present in the market for MVPD programming.

A close reading of Professor Rogerson's report and the JCC comments suggests that their real complaint is that broadcasters are being successful in their competition with vertically integrated MVPD networks to produce and market MVPD programming, i.e., that the "bundling" of which they complain is simply that broadcasters are producing and successfully marketing both broadcast and cable programming. But the success of

⁶⁷ For example, his result holds for products with independent demand only if the seller is able to pre-commit never to unbundle the goods in future periods. Such pre-commitment would not be possible in the market for television programming, where contracts are negotiated every three years. (See Whinston at 841-46.)

⁶⁸ Even Professor Nalebuff, one of the leading exponents of anticompetitive theories of product bundling, concedes that "There is often a presumption that firms can leverage power from one market to another. The Chicago School argument provides some surprisingly general conditions under which such leverage is not possible. It is particularly difficult to increase profits by using monopoly power to create leverage into competitive markets." (See Nalebuff 2003 at 19.)

broadcasters in the MVPD programming marketplace is almost certainly the result of economic efficiency, as Professor Rogerson explains in his report:

[T]here are significant 'economies of scope' for the networks between producing programming for their own use and producing programming that can be shown on MVPD networks. Once the networks were acquiring and/or producing significant amounts of content for use on their broadcast outlets, they found that they could use substantial amounts of in-house content that already existed and produce additional content at a relatively low incremental cost for distribution on affiliated MVPD networks. In many cases, this gave them a competitive advantage over other rivals....⁶⁹

Thus, he concludes,

[T]he networks would have entered the MVPD network programming industry to some extent regardless of whether or not retransmission consent had been enacted.⁷⁰

On these points we agree with Professor Rogerson entirely.

IV. SUMMARY AND CONCLUSIONS

In summary, JCC and Rogerson misapprehend both the cause and the effect in this matter. With respect to the effect, it simply is not the case that cable television prices are rising rapidly, or that MVPDs are being forced to carry networks consumers do not want to watch. Quality-adjusted prices are rising less rapidly than inflation, and consumers are watching more cable television every year.

With respect to cause, retransmission consent does not lead to anticompetitive effects in the market for MVPD programming. To the contrary, retransmission consent is nothing more or less than a *de facto* property right – the right of local broadcasters to benefit from the fruits of their investments in creating programming and packaging news

⁶⁹ Social Cost at 14-15.

⁷⁰ Social Cost at 17.

and entertainment for the benefit of consumers. Such property rights are essential for, not an obstacle to, the creation of efficiently functioning competitive markets.